Exhibit 9

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Delta Air Lines' CEO Discusses Q2 2012 Results - Earnings Call Transcript

Executives

Jill Greer – Managing Director, IR

Richard Anderson – CEO

Ed Bastian – President

Paul Jacobson – SVP and CFO

Glen Hauenstein – EVP, Network Planning & Revenue Management

Mike Campbell – EVP, Human Resources & Labor Relations

John Walker – SVP, Corporate Communications

Analysts

Glenn Engel – Bank of America

Savanthi Syth – Raymond James

Jamie Baker – JP Morgan

Dave Fintzen – Barclays

Mike Linenberg – Deutsche Bank

John Godyn – Morgan Stanley

Dan McKenzie – Rodman & Renshaw

Helane Becker – Dahlman Rose & Company

Kevin Crissey – UBS

Hunter Keay – Wolfe Trahan

Mary Schlangenstein – Bloomberg News

Andy Compart – Aviation Week

Josh Freed – The Associated Press

Kelly Yamanouchi – The Atlanta Journal-Constitution

Edward Russell – Flight Global

Linda Loyd – The Philadelphia Inquirer

Delta Air Lines, Inc. (DAL) Q2 2012 Earnings Call July 25, 2012 10:00 AM ET

Operator

Good morning ladies and gentlemen and welcome to the Delta Air Lines June 2012 Quarter Financial Results Conference Call. My name is Vicky and I will be your coordinator. (Operator Instructions) I would now like to turn the call over to Ms. Jill Sullivan Greer, Managing Director of Investor Relations for Delta. Please go ahead.

Jill Greer

Thanks, Vicky. Good morning everyone and thanks for joining us on our June quarter call. Speaking on the call today are Richard Anderson, Delta's Chief Executive Officer; our President, Ed Bastian; and our Chief Financial Officer, Paul Jacobson. We have the remainder of the management team here in the room with us for the Q&A. Richard will open the call. Ed then will address our financial and revenue performance and Paul will conclude with a review with a review of cost performance and liquidity. To get in as many questions as possible during the Q&A, please limit yourself to one question and a brief follow-up.

Today's discussion contains forward-looking statements that represent our beliefs or expectations about future events. All forward-looking statements involve risks and uncertainties that could cause the actual results to differ materially from the forward-looking statements. Some of the factors that may cause such differences are described in Delta's SEC filings. We'll also discuss non-GAAP financial measures and all results exclude special items unless otherwise noted. You can find the reconciliation of our non-GAAP measures on the Investor Relations page at delta.com.

And with that I'll turn the call over to Richard.

Richard Anderson

Thanks Jill. Good morning and thank you for joining us. This morning we announced a $586 million profit for the June quarter excluding special items, which is a $220 million improvement over last year. This represents EPS of $0.69 compared to consensus estimates of $0.68. Top line revenue grew 6%. Passenger unit revenues improved 8.5%.

Delta has now produced a unit revenue premium to the industry for 15 consecutive months, and we intend to continue doing so. Our 9.1% operating margin improved more than 200 basis points over last year and we have now achieved $5 billion of our $7 billion net debt reduction target. We will continue to reduce our debt and expect to get below $10 billion in net debt by the end of 2013.

Delta's operational performance for the quarter was exceptional. For the quarter, our completion factor was 99.7% and 87.5% of our flights arrived on time, an 8 point improvement over last year and our best ever June quarter operational performance. On top of that, our DOT mishandled baggage rate decreased 30% and our DOT customer complaints fell 20%. These results, combined with our international operational performance put Delta at the very top of the industry for operating performance and customer service.

By all measures these are some of the best financial and operational results in Delta's history, and I am thankful for the Delta team that has produced them. It is their commitment and dedication to this airline and our customers that differentiates Delta.

Looking forward, we are expecting to achieve a 10% to 12% operating margin in the September quarter, with system capacity forecast to be down 1% to 3% year-on-year. The revenue environment remains solid for Delta as July unit revenues are expected to increase 4% to 5% in each of our entities, Domestic, Latin, Pacific and Atlantic have good bookings in the third quarter. Capacity discipline is our key lever. We will continue to actively manage our capacity, including a 5% Trans-Atlantic capacity reduction for this fall. We will remain diligent in our efforts to have our fares fully reflect our costs and we will further reduce capacity if necessary to be certain we properly match our capacity with demand.

We're pleased with this quarter results and our outlook for 2012. We now have a unique opportunity to lay the

foundation for Delta's future with the continuing a number of strategic investments. These investments in our fleet network and facilities will pressure our costs in the near-term, but they are the right path to future margin gains as we have shown 2010, 2011 and 2012 with our financial performance.

The first investment we are making is to restructure our domestic fleet by eliminating a substantial portion of our 50-seat regional jet fleet. We've already completely retired our propeller fleet. We will ultimately replace 75% of our 50-seat flying with more cost-effective mainline aircraft and two-class regional jets. Our 50-seaters peaked at more than 500 in 2008 and we intend to reduce it to less than 125 aircraft over the next two years.

With the benefits achieved with our new pilot agreement, we have the flexibility we need to both accelerate our fleet restructuring and improve pilot productivity as we vary our capacity by season. The agreement enables us to up-gauge our domestic fleet by acquiring 717s and two-class regional jets which will replace more than 200 50-seat aircraft over the next few years.

On the network side, we're investing in New York where earlier this month we completed the largest expansion in the last 40 years at LaGuardia, predating that airport's first true connecting hub with more than 260 departures a day to 60 cities. We have experienced a 2% margin increase with an 18% increase in capacity at LaGuardia. Our expanded Terminal 4 at JFK joins the Atlanta International Terminal which opened this past May and our renovated LaGuardia complex in Terminal C and D will open at the end of the year.

We closed on the Monroe refinery transaction in this quarter. We have set up a separate Board of Directors and recruited a fine team of refining professionals under the leadership of our CEO, Jeff Warmann. We are in the turnaround process and expect to be operational in the September to October timeframe. As we stated, we expect the refinery to improve our operating results by approximately $300 million a year. Our intention is to improve our profitability with these gains. We will not use our refinery results to seek out market share. This is a unique opportunity for Delta that will bring significant advantage to Delta shareowners.

With all of these investments, we are making significant progress in becoming the airline of choice for our customers, particularly our business customers. This progress was reflected not only in our strong revenue performance and operational performance over the last year, but also in the recent J.D. Power survey in which Delta was the only carrier to significantly improve its overall score.

So to summarize, we're pleased with our progress, but there is still much more opportunity to build a much stronger Delta for our shareholders, employees and customers. Here's what you can expect to continue to see from us. We will continue to drive a significant RASM premium to the industry. We will provide a superior product and experience to our customers. We will be responsible in managing our capacity to be certain we've fully covered the cost of goods sold over the long term. We will aggressively manage our costs with a target of $1 billion in structural cost reduction over the next several years. We will pay down debt and de-lever our balance sheet. We will leverage our refinery acquisition to improve our results for our shareholders by at least $300 million a year. We will maintain a unique and an industry leading employee relations which will de-risk the business for our shareowners.

With that, I'll turn the call over to Ed. Thank you for your attention this morning.

Ed Bastian

Thanks Richard. Good morning everyone. Excluding special items, Delta reported net income of $586 million for the June quarter or $0.69 per share, $0.01 ahead of First Call consensus. Our operating margin for the quarter was 9.1%, up 2.2 points year-over-year.

We had $754 million of special items in the June quarter which resulted in a $168 million GAAP loss. Special items included $171 million for severance and related costs from our early retirement program in which over 2,000 employees elected to participate, $22 million in facilities and fleet charges, and a $561 million mark to market adjustment on fuel hedges, which reversed prior gains and moved our hedge book to a net $250 million loss position at the end of June.

Fuel prices have risen since the end of the quarter. And at current prices, the expected value of the hedge book sits at a $100 million loss. Looking forward, we expect to have negligible impact on a settlement basis as you can see in our fuel guidance of $3.09 per gallon for the September quarter and $3.05 per gallon for the December quarter.

Before I go through the revenue results, I would like to echo Richard's comments in thanking the Delta team for all of their great work that went into producing this quarter's results.

For the June quarter, turning to revenue, our top line revenues increased $580 million or 6% on a 1.3% decline in capacity. Passenger unit revenues increased 8.5%, driven by strong performance across all regions. I’m pleased to say that June marks the 15th consecutive month that we’ve generated a unit revenue premium to the industry, with our system unit revenues coming in at 105% of the industry average. This is the proof that we continue to see returns from the investments we’ve made in our products and our service.

Our Domestic unit revenues increased 8% on a 1 point reduction in capacity despite the negative impact from some competitive fare actions. Our expanded LaGuardia flying is doing quite well, resulting in a 2 point operating margin improvement on an 18 point increase in capacity. It’s very early, but we’re quite optimistic with the LaGuardia expansion.

In the Trans-Atlantic, our unit revenues improved 9% against a 7 point reduction in capacity, as we trimmed underperforming markets to better match demand. In spite of weak economic conditions in Europe, we saw good point of sale demand from our corporate customers in Europe as European businesses and investors showed interest in the relatively stronger US marketplace.

Specific unit revenues increased 9% for the quarter on a 10 point increase in capacity. We saw particularly strong improvements in load factor and yield for our in Trans-Pacific flights. In Latin America, we had an 8 point year-over-year improvement in unit revenue on flat capacity. While we saw some pressure from targeted sale fares, the region’s revenue performance remains strong, particularly in Mexico, which had a 25% unit revenue improvement.

On the corporate side, we continue to see momentum with corporate revenues for the quarter coming in at 14% year-over-year improvement, driven by a 1.5 point improvement in overall corporate travel share and good growth in automotive, financial service and healthcare sectors.

In terms of our revenue outlook, as we head into the September quarter, the revenue trends appear solid despite the continuing weak economic backdrop we face. For the month of July, we’re expecting our unit revenues to increase 4% to 5% and we continue to see unit revenue expansion across all entities, however, not at the rates we’ve seen over the last couple of years.

Comparisons continue to get more difficult as we proceed through the year. And while we welcome a reduction in fuel prices, it will likely be accompanied by some reduced yields as well. I’ll also remind you that the September quarter last year included a $70 million benefit from the FAA excise tax suspension.

Domestic bookings are trending well for July and August and we’re encouraged by the market’s continued response to our enhanced LaGuardia schedule. In the Pacific, which traditionally peaks in the September quarter, we see strong unit revenue performance for July and August, especially on our Trans-Pac flights into Japan. We’re looking at good booking trends in our Latin entity, with booked load factors showing improvement for every month up through the fall. And in the Trans-Atlantic, our aggressive management of off-peak capacity is helping us maintain solid book load factors.

In terms of the corporate revenue outlook, we recently surveyed our corporate clients to gauge their forecasted travel spend for the balance of the year, and 84% responded that they anticipated either the same or increased travel spend on Delta despite the relatively weak economy and global pressures, so corporate revenues continue to perform well.

Turning to guidance, we’re forecasting a profitable September quarter with an operating margin of 10% to 12%.

On capacity, we expect system capacity to be down 1% to 3% with domestic flat to down 2%, and our international capacity to be down 3% to 5%, driven by the previously announced post Labor Day capacity reductions in the Trans-Atlantic.

With, that I’ll now turn the call over to Paul.

Paul Jacobson

Thanks Ed. Good morning everyone and thank you for joining us this morning. Looking at our cost performance, our June quarter non-fuel unit costs increased 3.6% on a 1.3% decline in capacity, and as we’ve said, we expect our September quarter non-fuel unit costs to be up 5% to 6% versus prior year.

We are continuing to experience cost pressures from the impact of our 2% capacity reduction in the second half of

2012, as well as the enhancements we've made in our products, services and facilities which account for the majority of September quarter's cost growth. While pressure and costs in the near near-term, these service enhancements are strategic and do provide us a platform for our future success through expanded margins. Our opportunities for cost reductions lie in the structural initiatives we are implementing. These initiatives will take some time to begin delivering results, but they are unique opportunities to improve our cost outcomes.

First, the combination of our new pilot contract and this acquisition of the 717s allows us to accelerate our domestic fleet restructuring. We expect the 717s and the new 737-900ERs that begin delivering next year as well as bringing in 21 additional low capital MD-90s will allow us to retire older mainline aircraft and at least 200 50-seat regional jets over the next two to three years.

The retirement of the 50-seat regional jets is one of the single biggest opportunity costs we have. The up-gauging strategy will improve our efficiency by lowering our unit costs while simultaneously improving our product while maintaining our capacity discipline. Secondly, we are aligning our head count with our reduced capacity and recently had over 2,000 employees elect to participate in our voluntary early retirement program. These employees will retire by the end of the year with limited backfill, which will continue to result in improved productivity.

In addition, technology is also a critical key to improving our costs, whether through lower distribution costs or improved employee productivity. To that end, we've been making targeted technology investments in areas such as delta.com, crew scheduling systems and airport technology investments that not only will reduce costs in the future but will offer our customers better service. So we understand there's a lot more work to be done on our cost structure, but we're putting the pieces in place now to improve our cost outcomes in the future.

Turning to fuel, on a per gallon basis, Delta paid $3.37 per gallon for fuel for the quarter which includes $0.16 associated with hedge losses during the quarter. We entered the June quarter with a hedge book that was structured to protect against increases in oil prices up to $150 a barrel.

We remain committed to our hedging strategy and we view our hedge portfolio as protection from volatility in the fuel markets. We don't expect our hedge book to be a profit center but as a means to better manage our business by reducing the volatility of our largest expense. Based on the July 23 market close, as Ed mentioned, we are now projecting our fuel price to be $3.09 for the September quarter and $3.05 for the December quarter which includes minimal hedge impact and excludes any benefits from operating the refinery.

We are also looking at other initiatives like the refinery to reduce our fuel expense. As Richard mentioned, we closed on the purchase of the Trainer refinery in June and we expect initial start-up to occur in mid-September. We do expect the refinery will have a modest loss in the September quarter as we ramp up operations, but the refinery should be profitable, thereby reducing Delta's fuel expense beginning in the December quarter.

Turning now to liquidity, we ended the June quarter with $5.3 billion in unrestricted liquidity, including $1.8 billion in un-drawn lines of credit. We had $350 million of hedge collateral posted with counterparties at the end of the quarter, which was down to less than $100 million at Monday's close. We generated $683 million in operating cash flow in the quarter which was net of $354 million of pension funding. We have now completed all of our defined benefit funding for 2012.

We had $650 million in capital expenditures for the quarter which included $180 million for the Trainer refinery purchase, $65 million investment in Aeromexico and an additional $300 million in aircraft parts and modifications.

During the quarter, we paid down another $374 million in debt and ended the quarter with an adjusted net debt of $12.1 billion, well on our way to hitting our goal of $10 billion next year.

In the first week of July, we took advantage of favorable market conditions and completed the 2012-1 EETC, which priced $480 million at a very attractive 5.3% average interest rate. The proceeds of this offering will primarily be used to refinance the 2002-1 EETC, which matured in early July.

For the September quarter, we expect capital spending to be $400 million to $450 million and we have debt maturities of $200 million net of the proceeds of the EETC we just issued. And we are forecasting $5.1 billion of unrestricted liquidity at the end of September quarter.

In conclusion, Delta had a successful June quarter. We produced an operating margin of 9.1%, generated a revenue premium to the industry for the 15th consecutive month, and had exceptional operating performance. We've made strategic investments in the business which will generate margin increases into the future, and we are implementing the

structural initiatives we need to achieve better cost outcomes.

In conclusion as Richard and Ed mentioned earlier, these results would not have been possible without the hard work of our employees and all the momentum they've built into the business on all fronts.

Jill Greer

Thank you, Richard, Ed and Paul. Vicky, we're now ready to move to the questions from the analysts, so if you could please review the process for asking a question.

Question-and-Answer Session

Operator

Thank you, Ms. Greer. (Operator Instructions) We will take our first question from Glenn Engel of Bank of America.

Glenn Engel – Bank of America

Good morning. One cost question, one revenue question. On the cost side, the maintenance levels just, expense seems much higher than I would have expected. How long does it stay at these levels? In the second half, what do you expect it to level out at and what's normal?

Paul Jacobson

Glenn, we continue to experience some pressure from seat-related modifications in the second quarter. We expect maintenance spend to be roughly flat for the rest of the year.

Glenn Engel – Bank of America

Flat with last year or flat with the first half?

Paul Jacobson

Flat with last year.

Glenn Engel – Bank of America

And second is the timing of the July 4 holiday seemed to have had an impact for some airlines. Can you say how much that probably held back your July PRASM?

Glen Hauenstein

This is Glen. Glenn, how are you?

Glenn Engel – Bank of America

Good.

Glen Hauenstein

July 4 with falling on a Wednesday is clearly not good for airline revenues. Business travel really took the whole week off. And because it was on a Wednesday, the discretionary traveler demand was not as high as it would have been had it been at the beginning or the end of the week. So it was, it's generally a bad week for us. This year it was particularly bad and probably had about a 0.3 to 0.4 point impact on the month.

Glenn Engel – Bank of America

Thank you very much.

Richard Anderson

Thank you, Glenn.

Operator

Next we'll hear from Savanthi Syth, Raymond James.

Savanthi Syth – Raymond James

Good morning. Just wondering on the $300 million savings you're expecting for the refinery, could you provide a little bit more about how you get that? Or if the details are a little complicated, what drives that? What are the key inputs that drive it and given where the fuel prices have been volatile and pulling down, does the benefit reduce if fuel prices pull back, or what are the kind of key inputs in getting that $300 million in savings a year?

Paul Jacobson

Savi, the $300 million in savings comes from the sale of the products in excess of the cost of manufacturing and cracking crude oil against the index prices that we've seen. And while there's been volatility in the crude oil markets, crack spreads have actually expanded slightly during that time period and we don't anticipate any change from our original guidance.

Ed Bastian

Savi, this is Ed. One other point is we talked about this when we announced the acquisition. We went, also back-tested this over the last six years and the average return Trainer would have had on our results is anywhere between $300 million and $500 million a year over the last six years. So we feel reasonably confident in our estimates on a going forward basis.

Savanthi Syth – Raymond James

Great. Just on my follow up question, have you kind of calculated what the contribution will be with the replacement of 717s with the – or with the 50-seaters and the kind of older aircraft and what the timing of that would be?

Ed Bastian

We haven't publicly disclosed the impact. Obviously we believe it to be substantial. If you look at the, not just the cost of continuing to keep the 50-seat RJs in the fleet but even more importantly the upcoming fairly significant maintenance costs that we're going to be experiencing which will run into the hundreds of millions of dollars on that fleet if we had decided to retain that aircraft. So not just a savings on the current cost structure but a substantial benefit to offset future cost rises.

Savanthi Syth – Raymond James

All right. Great. Thank you.

Operator

Next we'll hear from Jamie Baker with JP Morgan.

Jamie Baker – JP Morgan

Hey, good morning everybody. Ed, the 16% of corporate accounts that responded they would be flying less, any color on what type of business they fall into and is that 16% of respondents or 16% of your corporate revenue base?

Ed Bastian

It was 16% of our respondents. We took a very wide span of respondents and it lined up largely with the spend. And in any portfolio, you're going to have some guys that are increasing, some guys that are decreasing some of the sectors. You can guess yourself which are having more difficulty in this marketplace, particularly in the defense space. But on average, the trend lines are they're going to continue to stay with the spend patterns and the trends we've seen or actually look to expand it a bit going forward. So no unique comment in that 16%. I didn't see JPMorgan's results. So I don't know what they are telling you.

Jamie Baker – JP Morgan

Yes, to be decided. For Paul, the new pilot agreement includes a decrease in the profit sharing calculation. Is it reasonable to assume similar changes for non-union employees and if so, have those changes been made or should we leave the equation alone in our models for now?

Richard Anderson

Mike?

Mike Campbell

We have said to the non-union employees that the same adjustment in profit sharing will be made with them and that will be effective January 1 for next year.

Jamie Baker – JP Morgan

January 1. Okay, helpful. And lastly if I can squeeze one in for Richard. Once you get below the $10 billion net debt target, what's next?

Richard Anderson

What do you think should be next?

Jamie Baker – JP Morgan

Well I think the concern out there is that you're tempted to fall off the wagon and you go on some sort of a growth bender. That's not particularly my concern, but I hear it from investors all the time. On the other hand, there are pension issues that still need to be addressed. There's possible restoration of dividends, share buyback potential. I mean sort of take your pick and don't limit it to those.

Richard Anderson

Well first of all, we're not going to go – I mean I think we have demonstrated now for a number of years in a row a unique discipline around how we deploy our capital, and I think the 717 is a prime example of that and the MD-90 is a prime example of that. So we're not going to change that focus, because we think the most important thing we can do for our shareowners is de-risk and de-lever the business.

So we have some time to make that decision because we're scheduled to hit our net debt at $10 billion at the end of 2013. I think you can reasonably expect that no matter what we do, we're going to continue to grind down that net debt number, because that both improves our EPS quickly because it comes right out of non-op which benefits our shareholders significantly.

So I think no matter what, there are two principles and we have some time to discuss this with our investor base. But the first principle is we are not going to go, to use your term, we're not going on any benders around here, period, because we're incredibly focused on pay back of our capital investments and getting our ROIC target. And number two, you can count on us continuing to pay down debt in some form or fashion, even after we hit the $10 billion mark. Our ultimate goal, it's going to take us a while, is to get back to investment grade.

Jamie Baker – JP Morgan

Excellent. And you say take a while. Care to throw a year out there?

Richard Anderson

No, I don't care to throw a year out there.

Jamie Baker – JP Morgan

Okay. All right. Thanks for the clarity on that. That's a excellent response. I appreciate you letting me slide a third question in.

Richard Anderson

Do you have a fourth?

Jamie Baker – JP Morgan

No. That's okay. I'll turn it over to somebody else. Sorry.

Richard Anderson

I have another one for you. What's JPM's travel going to be? Are you going to try to get them to pick with us?

Jill Greer

I think she cut him off.

Operator

Next we'll hear from David Fintzen with Barclays.

Dave Fintzen – Barclays

Hey, good morning everyone. Just a question for Glen. You sort of mentioned the 5% premium on RASM that you're hitting today. I mean as you look out over the next couple of years with the puts and takes of the refleetings versus ongoing merger synergies on the revenue side, just how do you see that evolving? Is 105% your long term target in where you think you go or do you think there's upside from here on a relative basis?

Glen Hauenstein

We really believe that there's continued upside. The 105% is actually an amalgamation of all of the different entities, not all of which we have produced premiums today, but all of which we aspire to produce premiums over time and we think that that will drive the system-wide number higher over the longer term.

Dave Fintzen – Barclays

And so we should think of those as 105% sort of your target in every entity or in all – or is that, every entity has its own sort of expectation?

Glen Hauenstein

Every entity has its own expectations based on our gauge, our stage length, the market selections we fly. But I think it's safe to say that we think there is a couple of points of headroom, 2 to 3 points of headroom in the next couple of years that we could achieve.

Dave Fintzen – Barclays

Okay. That's helpful. And maybe a question for Richard, on your ROIC targets, just as you take a step back and think about the derisking and the deleveraging, and how should we think about ROIC over the cycle? I mean is that, is the range shrinking? Do you think 10% to 12% is achievable in most environments or do you think there's still a pretty wide range on returns through the cycle?

Richard Anderson

What we've been able to show, I think if you look at 2010, 2011, now 2012, we've been able to manage and have good performance and make good money through three years of pretty volatile fuel and economic environment. So that 10% to 12% return on invested capital we think is a solid number for us going forward. And this is a management team that is incredibly serious and intent on hitting that number for our shareowners.

Dave Fintzen – Barclays

Okay. Appreciate that color.

Operator

Next we'll hear from Michael Linenberg with Deutsche Bank.

Mike Linenberg – Deutsche Bank

Yes, hey. Just a couple here and I guess maybe a clarification. Richard, in your opening comments, when you talked about the third quarter and you mentioned bookings being good, I thought I heard 4% to 5% top line growth. Was that in reference to the third quarter?

Richard Anderson

No.

Ed Bastian

Mike that was month of July RASM.

Richard Anderson

Yes.

Mike Linenberg – Deutsche Bank

Okay, okay. All right, so that's helpful then. I guess next one for Paul Jacobson, you talked about the change in, or the RJ fleet, the shrinkage of that by 250 airplanes as being the single largest opportunity cost. And again I realize that there's been some questions on this maybe sort of variations on this, but how do we think about this? I mean you talked about hundreds of millions of maybe foregone maintenance expense on some of the older aircraft. What about the potential revenue opportunity? There are a lot of different moving parts on this. Any additional color that you could give us would be great.

Ed Bastian

Mike, I'll jump in. This is Ed. The revenue opportunity is substantial. We've said any number of times the 50-seaters have been the perfect storm for us because not only is it a cost opportunity, it's also an airplane our customers don't particularly prefer. So as we up-gauge, and that was sitting behind the 717 strategy and that's why they are linked at some level as well as getting some incremental two-class 76-seat RJs, we're going to have a fairly substantial up gauge in margin improvement, cost reductions, some revenue enhancements. And from the capital efficiency standpoint, with where we were able to acquire the 717s is going to improve those returns all the more. So it was a win all the ways around.

Mike Linenberg – Deutsche Bank

Okay. All right, thank you. Very good.

Operator

Next we'll hear from John Godyn with Morgan Stanley.

John Godyn – Morgan Stanley

Hi, everyone. Thanks for taking my question. Richard, when investors think of Delta, I think increasingly they look at you as aggressive and creative at trying to better manage or control some of the forces that other airlines leave to chance and maybe best symbolized by the recent refinery deal, and that's something you touched on in your prepared remarks. But as we think about scenarios surrounding American's emergence and the possibility of M&A, is this a situation where you think the outcomes are out of your control or does Delta have the ability to drive the situation toward outcomes it favors?

Richard Anderson

As a matter of policy, we do not comment or speculate on transactions of that nature. I would just say that overall, one, at Delta we will continue to always control our destiny. And by pushing a lot of different opportunities and leverage across the business and, number two, global consolidation is good for the business model.

John Godyn – Morgan Stanley

Okay. That's helpful. And just broadly, we've heard from a lot of different airlines about solid revenue trends and how we're not seeing really any signs of economic weakness yet. But this quarter cargo revenue for you guys fell year-over-year for the second quarter in a row and we've seen a lot of weakness in cargo. Normally that's a canary in the coal mine. Can you help us understand why it makes sense to look through cargo weakness this time around when thinking about the trajectory of passenger revenue?

Ed Bastian

John, this is Ed. Cargo revenues for us in the second quarter were fairly flat on a year-over-year basis and we had some weakness in yields, but the volumes improved on a year-over-year basis. We're not a big enough cargo carrier to really be able to call that as a trend. Obviously we see what's going on with the bigger freight operators around the world. So I'd say, one, don't necessarily look at our cargo performance as a indicator.

But looking to our business model, we think when you're – because we've asked ourself that question a lot with some of the continued concerns and headline risk coming out of Europe and other parts of the geography, how do we look at our July unit revenue performance. And if you were to contrast June to July, there's about a 2 point sequential down-tick, which compared to what we would historically have expected to see. We think 1 point of the 2 point down-tick is due to some of the domestic competitive fare activities that we've commented on in the past.

And the other point is a myriad of a little bit of economic weakness, a little bit of the fuel sell-off which obviously has some revenue implications, a little bit of July 4. And again, just so a little bit of softening but nothing on the guise of what some of the cargo carriers are seeing. So, or a consumer business in the environment that we're operating in to see a 4 to 5 point year-on-year revenue improvement, which is our, effectively our same stores sales metric. We feel it's pretty solid.

John Godyn – Morgan Stanley

Okay, and can I ask just a quick clarification on an earlier question. There was a question about uses of cash and free cash flow. When you guys think about excess cash for paying down debt or what have you, is the right way to think about it as cash above and beyond the air traffic liability or do you define excess cash in a different way?

Paul Jacobson

We define excess cash as free cash flow, operating cash less capital investment.

John Godyn – Morgan Stanley

Okay. Thanks a lot.

Operator

Next we'll hear from Dan McKenzie with Rodman & Renshaw.

Dan McKenzie – Rodman & Renshaw

Hey, good morning everybody, thanks here. Ed, over what period of time is Delta targeting the $1 billion in cost savings and where does that leave the new non-fuel cost target? And then I guess related to that, how are you thinking about full year cost guidance at this point?

Ed Bastian

The $1 billion structural cost reduction is over the next two to three years, Dan, and obviously the 50-seat reduction is probably the single biggest contributor there. But the early retirement package that we just completed is also a contributor, so it will take a couple of years to see the benefits come through.

Dan McKenzie – Rodman & Renshaw

I see. And then I guess secondly here, if I can go back to revenues at 10% to 12% operating margin for the third quarter, of course is pretty encouraging. But the investor worry is just the daily barrage of negative economic data points and historically revenues at times have deteriorated quite quickly. I wonder if you could just talk about what's different today. Can you elaborate a little further about the source of confidence as you look ahead to demand in the back half of the year?

Glen Hauenstein

This is Glen. How are you doing?

Dan McKenzie – Rodman & Renshaw

Yes, thanks, Glen.

Glen Hauenstein

We don't have a crystal ball here and I think our commitment is to react as quickly as we can to changes in demand, and as we look out into the early fall, we really don't see anything yet. But that doesn't mean that we won't react quickly if we do see a shortfall. So I think our commitment to our shareholders and all of our constituents is to make sure we're doing the best we can with the information we have. And while we read the same headlines, right now in Europe we have a little bit of a disconnect between what we're experiencing and what you read in the headlines. So, and the forward bookings and forward unit revenues look great into the fall. If that starts to deteriorate, and so we have already taken proactive reductions. So we have reduced 5% of our capacity because of things we know. So we know the euro is lower and we know that winter is higher ex-European demand than ex-US demand which peaks in the summer. So we've already taken actions on what we know, and we will take the actions required as more unfolds if it does.

Dan McKenzie – Rodman & Renshaw

Okay, terrific. Thanks so much.

Operator

Next we'll hear from Helane Becker with Dahlman Rose & Company.

Helane Becker – Dahlman Rose & Company

Thanks very much, operator. Hi everybody. So just with respect to the changes you're going to make over on the regional side, one of your major providers is basically out there saying that there's no way you can get out of their contract, and the contracts go out four or five more years. And I'm just kind of wondering how we should think about that, given the fact that you've got to get down to something like 125 50-seaters over the next I think three years.

Richard Anderson

Well we have, without going into the particulars of any of the contracts that we have, we have a steady path to be able to get to 125. So we, without going into the specifics, we have a confident path of moving to the 125 and I'll just leave it at that.

Helane Becker – Dahlman Rose & Company

Okay. I will accept that. And then my other question is with respect to Latin American market. In the past couple of months, I've just seen some unit revenue growth slow. It hasn't been quite as robust as it was six or eight months ago. Is there anything accounting for that or is it just tougher comps which would be one thing to account for, I suppose. But is there anything going on we should know about?

Glen Hauenstein

This is Glen again. If you look to the fall, I think the one thing that we are keeping a close eye on is industry capacity. Clearly not Delta capacity, but as you get into the fall in Latin America, current schedules show that capacity is up around 10%. You combine that with decline of the local currencies, the real now, a lot of the real is not priced, the tickets aren't priced in reals but about 10% of our Brazilian sales for example are priced in reals and that has a 30% negative year-over-year bias. So I think you've got some foreign exchange. I think you've got some capacity issues. But I think the core demand is still quite strong.

Helane Becker – Dahlman Rose & Company

Okay. And then your investments in Aeromexico, where does that show up in the numbers, or does it?

Ed Bastian

It wouldn't show up, Helane, in the numbers per se. It would show up through better passenger revenues as we better hook our two networks up. You're not going to see that in a separate line item or anything.

Helane Becker – Dahlman Rose & Company

Okay, got you. Thank you.

Operator

Next we'll hear from Kevin Crissey with UBS.

Kevin Crissey – UBS

Hi. Thanks for taking my questions. CASM ex-fuel, I guess I just wanted to go back over the timeline a little bit. I think it was back say maybe October 2010, I think it was somewhere in that vicinity, you guys had targeted 2011 to be kind of flat with 2010. And then I think it was revised at your Investor Day and then you've cut some capacity. But what I'm trying to understand is, I didn't see these CASM ex-fuel pressures coming and I think I didn't see them partly because I think you guys had guided that they weren't really there or at least one point you had guided it that way, or maybe I'm misreading it. But I wanted to understand what changed from that point to today in terms of your pressure on the CASM ex-fuel line.

Richard Anderson

This is Richard. First, if you look out over the past two years, we have pushed capacity down pretty hard. We have viewed capacity as the real lever to push our business, and it has put real pressure on our non-fuel CASM. If you look

where we'll be by the end of this year in 4Q and compare it to two years ago when we were giving that guidance, we're going to probably be down 5% to 6% in overall system capacity and the industry is probably on the main grown a bit. So if you think about being down 5% instead of being up 1% to 2% each of those two years, the equation is very much different on the nonfuel line.

The second piece is, is that we have along the way made investments that are the right investments in our product, in our employees, and you can see it in our revenue performance versus the industry. Hence our drive to drive another $1 billion of structural costs out and our push in the refinery to make up on a total basis, total unit cost basis, those inflationary pressures that we see.

Ed Bastian

And I'd say the other thing, Kevin, there that we did not necessarily forecast or see coming as clearly is the opportunity we had with our pilots to do the contract early. It's going to pay significant dividends over time as it will have a big cost return to it, not just in terms of improved productivity, but the ability to fairly substantially restructure the domestic fleet. But that those costs came in right away so that's in our September guidance as well, and that was another big piece.

Kevin Crissey – UBS

Okay. Thank you. And Richard maybe if I think about, you talk about derisking the business and we all want that, one of the big things as we look across transportation companies, fuel is only a discussion in the airlines pretty much. If you look at trucking or rails and stuff, what more can be done to allow fuel surcharges to truly be pass-throughs? I mean it should be to me, it should be the effort that's expended by every company before they buy more planes, it's like let's see how we can get a fuel surcharge in here that actually truly does what it does in every other industry.

Richard Anderson

Two points there that are different in this industry from those industries, which is we sell our tickets 330 days in advance. So if at the point in time that we sell the ticket for travel six months from now, we don't have – we have current fuel or the current forecast that we have for fuel which we use in our pricing department.

Because, if you look at businesses in a totally deregulated environment that are commodity intensive, the management team is always working to match the cost of production to the pricing in the marketplace. We're a bit more challenged in that we sell tickets 330 days in advance and the DOT does not allow us to collect fuel surcharges in the US. We can inform point of sale but we cannot in the US.

So there are some differences there. So what we do is we manage capacity very tightly and are prepared to suffer some of the risks of a little higher unit cost creep as a result because the independent variable needs to be then how we manage our capacity and how we manage our internal pricing mechanisms to be certain that our prices are capturing the actual cost of goods sold at the time that we price.

And that leads me to my second point which is why we hedge fuel. Because if you're selling 330 days in advance and you cannot legally use fuel surcharges, we need the ability to take some of the volatility out and allow us in a more near term basis to lock in our margins.

And candidly, that's what we just did in the second quarter. When we were moving through the second quarter, we saw some of the best revenue performance we've ever seen for the month of May, and but the biggest risk was where fuel was going in the January through April timeframe. And we wanted to be certain that we had 200 basis points of margin expansion. So it's going to be a combination of, one, managing your capacity, because that's our biggest lever. And we're going to continue to manage the capacity to be able to drive our revenue up by putting more revenue on each airplane and you do that by reducing capacity.

The second thing is, in our pricing environment, we're very focused on having our pricing and yield management professionals have the cost data at the time they make decisions around capacity and pricing. Third, we made an investment in the refinery to be able to take the crack spread risk out of our business, which is our single highest fuel expense. And number four, to use our hedging program in the shorter term to be able to lock in our margins, so that we know that our cost of goods sold is going to match the pricing we have in the market.

Kevin Crissey – UBS

Thank you. Just one last real fast one because Jamie had three, I'll take three. Capacity change by month, if you could to help us frame the RASM expectations by month?

Ed Bastian

There's nothing – we don't typically give the monthly forward capacity outlooks, Kevin, but there's nothing unique in the months.

Kevin Crissey – UBS

Okay. Thank you.

Jill Greer

Vicky, we're going to have time for one more question from the analysts.

Operator

Okay. We will take our question from Hunter Keay with Wolfe Trahan.

Hunter Keay – Wolfe Trahan

Thanks for getting me in, appreciate it. Just maybe a subtlety, Richard, but you've referred to a net debt target of $10 billion by the end of 2013. I think recently you guys have been saying mid-2013. Is there any particular reason why that's changed? Given I think the pull back in the fuel prices, I would have thought maybe that could have been possibly even accelerated a little bit. Is that, just any kind of color on that would be great.

Richard Anderson

No, there's no change. Our goal is to make certain that we get it done as soon as possible.

Hunter Keay – Wolfe Trahan

Sure, okay thanks. And a little bit more on the hedge book. Can you tell us how you manage the risk or oversee the tail risk in the hedge book? Because we obviously saw some pretty big mark to market adjustments with the big pull back in prices in May and I'm wondering how you guys think about managing risk within the derivative exposure in the hedge book. Who oversees it, what's your sort of tolerance threshold for risk? Any kind of color you could share with us would be great.

Paul Jacobson

Hunter, this is Paul.

Hunter Keay – Wolfe Trahan

Hey Paul.

Paul Jacobson

We have a robust and independent risk management function that oversees the financial risks of the company including the hedging book. When we hedge fuel and we see rapid declines in fuel prices, you're going to expect hedge losses because the hedge book is net long in its offsetting position. But we monitor that very independently and we're very comfortable with our position in our book.

Hunter Keay – Wolfe Trahan

Okay. Thank you.

Jill Greer

Vicky, that is going to conclude the analyst portion of the call and so I'm going to turn it over to Ned Walker, our Chief Communications Officer for the media portion.

John Walker

Okay hey, thanks very much, Jill, and welcome everybody. Vicky, we're ready to begin the Q&A with the media. We'll ask the media to limit themselves to one question with a quick follow-up. We should be able to accommodate most Q&As but often we are not able to get everybody on. So with that we'll go ahead and turn it over to the first question, please.

Operator

Thank you. Again, that concludes the analyst portion of the question and answer session. We will now take questions from the media. (Operator Instructions) We'll take our first question from Mary Schlangenstein with Bloomberg News.

Mary Schlangenstein – Bloomberg News

Quick question. Earlier in the call, you said that you are looking at other initiatives like the refinery to decrease your fuel exposure. And I wanted to see if you could be any more specific in terms of what you might be looking at.

Richard Anderson

I thought we were fairly clear in saying that the way we manage our fuel exposure is, one, capacity; number two, having the right pricing processes and mechanisms in the company to be certain that we're fully covering the cost of fuel in our pricing; number three, we have a lot of fuel efficiency efforts under way, including our refleeting, adding winglets and more efficient aircraft routings; and then number four is our hedge program.

Mary Schlangenstein – Bloomberg News

I'm sorry. I thought the reference was perhaps to another asset purchase of some kind?

Richard Anderson

No, that was not what the reference was at all.

Mary Schlangenstein – Bloomberg News

Okay. Thank you.

John Walker

Thanks, Mary.

Operator

Next we'll hear from Andy Compart with Aviation Week.

Andy Compart – Aviation Week

Richard, I want to get back to the steady path to 125 50-seaters. SkyWest's CFO, which was an indirect reference made to earlier, had said to me that they operate about 150 50-seaters and he said they are not inclined to trade them for 76-seater, two-class 76 seaters if there's nowhere to put the 50-seater. So that's above 125 right there. so how do you get to that if SkyWest or others are resistant to making this trade-off?

Richard Anderson

I'm going to stand on what I said before which is we have a clear path through – we have a number of operators and a number of contract expirations and I think we've shown a pretty steady process here. I mean our high watermark was a little over 500 and I think today we're at 300, 320. So we've been able to do 180 so and I think you just have to stay tuned, but it's going to happen.

Andy Compart – Aviation Week

Can you do it without voluntary participation by some of the partners?

Richard Anderson

As I said, I mean without going into the specifics of any of these, it is going to happen.

Andy Compart – Aviation Week

All right. Thanks.

John Walker

Thanks Andy. Vicky, next question.

Operator

Next we'll hear from Josh Freed with The Associated Press

Josh Freed – The Associated Press

Yes, well I suppose this is related. What can you tell us today about your plans for Comair?

Richard Anderson

In view of the significant changes in the economic and competitive conditions in the regional airline industry in recent years, Delta continues to explore strategic alternatives for Comair as previously announced. Until a final decision has been made, we cannot comment further.

John Walker

Hey, thanks Richard that was really good.

Josh Freed – The Associated Press

It almost felt like you were reading from something there.

John Walker

No, that's really, Josh, that's really basically been what we've been telling you and the rest of the media over the last few weeks and so our position really hasn't changed publicly on that.

Josh Freed – The Associated Press

All right. Thank you.

Operator

Next we'll hear from Kelly Yamanouchi with The Atlanta Journal-Constitution.

Kelly Yamanouchi – The Atlanta Journal-Constitution

Hi there. I'm just wondering, since you have a target of $1 billion in structural cost reduction over the next few years, do you plan for further job cuts over that period to accomplish that?

John Walker

No.

Kelly Yamanouchi – The Atlanta Journal-Constitution

All right. Thank you.

Operator

Next we'll hear from Edward Russell with Flight Global.

Edward Russell – Flight Global

Yes, hi. I was wondering if you could detail a bit more the swap from 50-seaters to 76-seaters at your regional carriers about who might be receiving those and where they might be going?

Richard Anderson

No, we wouldn't comment on that. We've got a lot of work to do there and there will be RFP processes and the like so we can't comment on that. We'll let you know as soon as it's all worked out.

Edward Russell – Flight Global

Okay. Thank you.

John Walker

Okay Vicky, we have time for one more question

Operator

Okay, we will take that question from Linda Loyd with Philadelphia Inquirer.

Linda Loyd – The Philadelphia Inquirer

Thank you for taking my call. I have two questions about the Trainer refinery. How is the turnaround at Trainer going at this point, and do you anticipate you will have to spend more than the estimated $100 million to get the refinery up and running?

Paul Jacobson

This is Paul Jacobson. The turnaround is actually progressing very, very well. We are on budget and on target to begin restarting that facility in mid-September, and we expect the actual costs to come in line with all of our expectations. There have been no surprises.

Linda Loyd – The Philadelphia Inquirer

Well thank you, and I have one follow-up question. How many years are the swaps with BP and Phillips 66? That's the first part of that, and what are Delta's plans after those swaps expire?

Paul Jacobson

Those are, all the commercial agreements that we entered into are three-year agreements and we'll continue to monitor that as we get underway and down the road and explore our options.

Linda Loyd – The Philadelphia Inquirer

Because it is not true that the benefits of buying the refinery hinges on the swaps for the gasoline and diesel produced at Trainer for jet fuel that is made somewhere else?

Paul Jacobson

No, the swaps are a means to exchange product for jet fuel. The economics of the transaction don't hinge on those commercial agreements but they are sources for those products and there's a broad market for those products in that area.

Linda Loyd – The Philadelphia Inquirer

Okay. Thanks very much.

John Walker

Okay thank you very much, Richard, Ed and Paul. That concludes our June quarter call. We'll be back in three months with the September quarter. Thanks very much.

Operator

Again that does conclude today's teleconference. Thank you all for joining.

Executives

Jill Greer – Managing Director, IR

Richard Anderson – CEO

Ed Bastian – President

Paul Jacobson – SVP and CFO

Glen Hauenstein – EVP, Network Planning & Revenue Management

Mike Campbell – EVP, Human Resources & Labor Relations

John Walker – SVP, Corporate Communications

Analysts

Glenn Engel – Bank of America

Savanthi Syth – Raymond James

Jamie Baker – JP Morgan

Dave Fintzen – Barclays

Mike Linenberg – Deutsche Bank

John Godyn – Morgan Stanley

Dan McKenzie – Rodman & Renshaw

Helane Becker – Dahlman Rose & Company

Kevin Crissey – UBS

Hunter Keay – Wolfe Trahan

Mary Schlangenstein – Bloomberg News

Andy Compart – Aviation Week

Josh Freed – The Associated Press

Kelly Yamanouchi – The Atlanta Journal-Constitution

Edward Russell – Flight Global

Linda Loyd – The Philadelphia Inquirer

Delta Air Lines, Inc. (DAL) Q2 2012 Earnings Call July 25, 2012 10:00 AM ET

Operator

Good morning ladies and gentlemen and welcome to the Delta Air Lines June 2012 Quarter Financial Results Conference Call. My name is Vicky and I will be your coordinator. (Operator Instructions) I would now like to turn the call over to Ms. Jill Sullivan Greer, Managing Director of Investor Relations for Delta. Please go ahead.

Jill Greer

Thanks, Vicky. Good morning everyone and thanks for joining us on our June quarter call. Speaking on the call today are Richard Anderson, Delta's Chief Executive Officer; our President, Ed Bastian; and our Chief Financial Officer, Paul Jacobson. We have the remainder of the management team here in the room with us for the Q&A. Richard will open the call. Ed then will address our financial and revenue performance and Paul will conclude with a review with a review of cost performance and liquidity. To get in as many questions as possible during the Q&A, please limit yourself to one question and a brief follow-up.

Today's discussion contains forward-looking statements that represent our beliefs or expectations about future events. All forward-looking statements involve risks and uncertainties that could cause the actual results to differ materially from the forward-looking statements. Some of the factors that may cause such differences are described in Delta's SEC filings. We'll also discuss non-GAAP financial measures and all results exclude special items unless otherwise noted. You can find the reconciliation of our non-GAAP measures on the Investor Relations page at delta.com.

And with that I'll turn the call over to Richard.

Richard Anderson

Thanks Jill. Good morning and thank you for joining us. This morning we announced a $586 million profit for the June quarter excluding special items, which is a $220 million improvement over last year. This represents EPS of $0.69 compared to consensus estimates of $0.68. Top line revenue grew 6%. Passenger unit revenues improved 8.5%.

Delta has now produced a unit revenue premium to the industry for 15 consecutive months, and we intend to continue doing so. Our 9.1% operating margin improved more than 200 basis points over last year and we have now achieved $5 billion of our $7 billion net debt reduction target. We will continue to reduce our debt and expect to get below $10 billion in net debt by the end of 2013.

Delta's operational performance for the quarter was exceptional. For the quarter, our completion factor was 99.7% and 87.5% of our flights arrived on time, an 8 point improvement over last year and our best ever June quarter operational performance. On top of that, our DOT mishandled baggage rate decreased 30% and our DOT customer complaints fell 20%. These results, combined with our international operational performance put Delta at the very top of the industry for operating performance and customer service.

By all measures these are some of the best financial and operational results in Delta's history, and I am thankful for the Delta team that has produced them. It is their commitment and dedication to this airline and our customers that differentiates Delta.

Looking forward, we are expecting to achieve a 10% to 12% operating margin in the September quarter, with system capacity forecast to be down 1% to 3% year-on-year. The revenue environment remains solid for Delta as July unit revenues are expected to increase 4% to 5% in each of our entities, Domestic, Latin, Pacific and Atlantic have good bookings in the third quarter. Capacity discipline is our key lever. We will continue to actively manage our capacity, including a 5% Trans-Atlantic capacity reduction for this fall. We will remain diligent in our efforts to have our fares fully reflect our costs and we will further reduce capacity if necessary to be certain we properly match our capacity with demand.

We're pleased with this quarter results and our outlook for 2012. We now have a unique opportunity to lay the foundation for Delta's future with the continuing a number of strategic investments. These investments in our fleet network and facilities will pressure our costs in the near-term, but they are the right path to future margin gains as we have shown 2010, 2011 and 2012 with our financial performance.

The first investment we are making is to restructure our domestic fleet by eliminating a substantial portion of our 50-seat regional jet fleet. We've already completely retired our propeller fleet. We will ultimately replace 75% of our 50-seat flying with more cost-effective mainline aircraft and two-class regional jets. Our 50-seaters peaked at more than 500 in 2008 and we intend to reduce it to less than 125 aircraft over the next two years.

With the benefits achieved with our new pilot agreement, we have the flexibility we need to both accelerate our fleet restructuring and improve pilot productivity as we vary our capacity by season. The agreement enables us to up-gauge our domestic fleet by acquiring 717s and two-class regional jets which will replace more than 200 50-seat aircraft over the next few years.

On the network side, we're investing in New York where earlier this month we completed the largest expansion in the last 40 years at LaGuardia, predating that airport's first true connecting hub with more than 260 departures a day to 60 cities. We have experienced a 2% margin increase with an 18% increase in capacity at LaGuardia. Our expanded Terminal 4 at JFK joins the Atlanta International Terminal which opened this past May and our renovated LaGuardia complex in Terminal C and D will open at the end of the year.

We closed on the Monroe refinery transaction in this quarter. We have set up a separate Board of Directors and recruited a fine team of refining professionals under the leadership of our CEO, Jeff Warmann. We are in the turnaround

process and expect to be operational in the September to October timeframe. As we stated, we expect the refinery to improve our operating results by approximately $300 million a year. Our intention is to improve our profitability with these gains. We will not use our refinery results to seek out market share. This is a unique opportunity for Delta that will bring significant advantage to Delta shareowners.

With all of these investments, we are making significant progress in becoming the airline of choice for our customers, particularly our business customers. This progress was reflected not only in our strong revenue performance and operational performance over the last year, but also in the recent J.D. Power survey in which Delta was the only carrier to significantly improve its overall score.

So to summarize, we're pleased with our progress, but there is still much more opportunity to build a much stronger Delta for our shareholders, employees and customers. Here's what you can expect to continue to see from us. We will continue to drive a significant RASM premium to the industry. We will provide a superior product and experience to our customers. We will be responsible in managing our capacity to be certain we've fully covered the cost of goods sold over the long term. We will aggressively manage our costs with a target of $1 billion in structural cost reduction over the next several years. We will pay down debt and de-lever our balance sheet. We will leverage our refinery acquisition to improve our results for our shareholders by at least $300 million a year. We will maintain a unique and an industry leading employee relations which will de-risk the business for our shareowners.

With that, I'll turn the call over to Ed. Thank you for your attention this morning.

Ed Bastian

Thanks Richard. Good morning everyone. Excluding special items, Delta reported net income of $586 million for the June quarter or $0.69 per share, $0.01 ahead of First Call consensus. Our operating margin for the quarter was 9.1%, up 2.2 points year-over-year.

We had $754 million of special items in the June quarter which resulted in a $168 million GAAP loss. Special items included $171 million for severance and related costs from our early retirement program in which over 2,000 employees elected to participate, $22 million in facilities and fleet charges, and a $561 million mark to market adjustment on fuel hedges, which reversed prior gains and moved our hedge book to a net $250 million loss position at the end of June.

Fuel prices have risen since the end of the quarter. And at current prices, the expected value of the hedge book sits at a $100 million loss. Looking forward, we expect to have negligible impact on a settlement basis as you can see in our fuel guidance of $3.09 per gallon for the September quarter and $3.05 per gallon for the December quarter.

Before I go through the revenue results, I would like to echo Richard's comments in thanking the Delta team for all of their great work that went into producing this quarter's results.

For the June quarter, turning to revenue, our top line revenues increased $580 million or 6% on a 1.3% decline in capacity. Passenger unit revenues increased 8.5%, driven by strong performance across all regions. I'm pleased to say that June marks the 15th consecutive month that we've generated a unit revenue premium to the industry, with our system unit revenues coming in at 105% of the industry average. This is the proof that we continue to see returns from the investments we've made in our products and our service.

Our Domestic unit revenues increased 8% on a 1 point reduction in capacity despite the negative impact from some competitive fare actions. Our expanded LaGuardia flying is doing quite well, resulting in a 2 point operating margin improvement on an 18 point increase in capacity. It's very early, but we're quite optimistic with the LaGuardia expansion.

In the Trans-Atlantic, our unit revenues improved 9% against a 7 point reduction in capacity, as we trimmed underperforming markets to better match demand. In spite of weak economic conditions in Europe, we saw good point of sale demand from our corporate customers in Europe as European businesses and investors showed interest in the relatively stronger US marketplace.

Specific unit revenues increased 9% for the quarter on a 10 point increase in capacity. We saw particularly strong improvements in load factor and yield for our in Trans-Pacific flights. In Latin America, we had an 8 point year-over-year improvement in unit revenue on flat capacity. While we saw some pressure from targeted sale fares, the region's revenue performance remains strong, particularly in Mexico, which had a 25% unit revenue improvement.

On the corporate side, we continue to see momentum with corporate revenues for the quarter coming in at 14% year-over-year improvement, driven by a 1.5 point improvement in overall corporate travel share and good growth in automotive, financial service and healthcare sectors.

In terms of our revenue outlook, as we head into the September quarter, the revenue trends appear solid despite the continuing weak economic backdrop we face. For the month of July, we're expecting our unit revenues to increase 4% to 5% and we continue to see unit revenue expansion across all entities, however, not at the rates we've seen over the last couple of years.

Comparisons continue to get more difficult as we proceed through the year. And while we welcome a reduction in fuel prices, it will likely be accompanied by some reduced yields as well. I'll also remind you that the September quarter last year included a $70 million benefit from the FAA excise tax suspension.

Domestic bookings are trending well for July and August and we're encouraged by the market's continued response to our enhanced LaGuardia schedule. In the Pacific, which traditionally peaks in the September quarter, we see strong unit revenue performance for July and August, especially on our Trans-Pac flights into Japan. We're looking at good booking trends in our Latin entity, with booked load factors showing improvement for every month up through the fall. And in the Trans-Atlantic, our aggressive management of off-peak capacity is helping us maintain solid book load factors.

In terms of the corporate revenue outlook, we recently surveyed our corporate clients to gauge their forecasted travel spend for the balance of the year, and 84% responded that they anticipated either the same or increased travel spend on Delta despite the relatively weak economy and global pressures, so corporate revenues continue to perform well.

Turning to guidance, we're forecasting a profitable September quarter with an operating margin of 10% to 12%.

On capacity, we expect system capacity to be down 1% to 3% with domestic flat to down 2%, and our international capacity to be down 3% to 5%, driven by the previously announced post Labor Day capacity reductions in the Trans-Atlantic.

With, that I'll now turn the call over to Paul.

Paul Jacobson

Thanks Ed. Good morning everyone and thank you for joining us this morning. Looking at our cost performance, our June quarter non-fuel unit costs increased 3.6% on a 1.3% decline in capacity, and as we've said, we expect our September quarter non-fuel unit costs to be up 5% to 6% versus prior year.

We are continuing to experience cost pressures from the impact of our 2% capacity reduction in the second half of 2012, as well as the enhancements we've made in our products, services and facilities which account for the majority of September quarter's cost growth. While pressure and costs in the near near-term, these service enhancements are strategic and do provide us a platform for our future success through expanded margins. Our opportunities for cost reductions lie in the structural initiatives we are implementing. These initiatives will take some time to begin delivering results, but they are unique opportunities to improve our cost outcomes.

First, the combination of our new pilot contract and this acquisition of the 717s allows us to accelerate our domestic fleet restructuring. We expect the 717s and the new 737-900ERs that begin delivering next year as well as bringing in 21 additional low capital MD-90s will allow us to retire older mainline aircraft and at least 200 50-seat regional jets over the next two to three years.

The retirement of the 50-seat regional jets is one of the single biggest opportunity costs we have. The up-gauging strategy will improve our efficiency by lowering our unit costs while simultaneously improving our product while maintaining our capacity discipline. Secondly, we are aligning our head count with our reduced capacity and recently had over 2,000 employees elect to participate in our voluntary early retirement program. These employees will retire by the end of the year with limited backfill, which will continue to result in improved productivity.

In addition, technology is also a critical key to improving our costs, whether through lower distribution costs or improved employee productivity. To that end, we've been making targeted technology investments in areas such as delta.com, crew scheduling systems and airport technology investments that not only will reduce costs in the future but will offer our customers better service. So we understand there's a lot more work to be done on our cost structure, but we're

putting the pieces in place now to improve our cost outcomes in the future.

Turning to fuel, on a per gallon basis, Delta paid $3.37 per gallon for fuel for the quarter which includes $0.16 associated with hedge losses during the quarter. We entered the June quarter with a hedge book that was structured to protect against increases in oil prices up to $150 a barrel.

We remain committed to our hedging strategy and we view our hedge portfolio as protection from volatility in the fuel markets. We don't expect our hedge book to be a profit center but as a means to better manage our business by reducing the volatility of our largest expense. Based on the July 23 market close, as Ed mentioned, we are now projecting our fuel price to be $3.09 for the September quarter and $3.05 for the December quarter which includes minimal hedge impact and excludes any benefits from operating the refinery.

We are also looking at other initiatives like the refinery to reduce our fuel expense. As Richard mentioned, we closed on the purchase of the Trainer refinery in June and we expect initial start-up to occur in mid-September. We do expect the refinery will have a modest loss in the September quarter as we ramp up operations, but the refinery should be profitable, thereby reducing Delta's fuel expense beginning in the December quarter.

Turning now to liquidity, we ended the June quarter with $5.3 billion in unrestricted liquidity, including $1.8 billion in un-drawn lines of credit. We had $350 million of hedge collateral posted with counterparties at the end of the quarter, which was down to less than $100 million at Monday's close. We generated $683 million in operating cash flow in the quarter which was net of $354 million of pension funding. We have now completed all of our defined benefit funding for 2012.

We had $650 million in capital expenditures for the quarter which included $180 million for the Trainer refinery purchase, $65 million investment in Aeromexico and an additional $300 million in aircraft parts and modifications.

During the quarter, we paid down another $374 million in debt and ended the quarter with an adjusted net debt of $12.1 billion, well on our way to hitting our goal of $10 billion next year.

In the first week of July, we took advantage of favorable market conditions and completed the 2012-1 EETC, which priced $480 million at a very attractive 5.3% average interest rate. The proceeds of this offering will primarily be used to refinance the 2002-1 EETC, which matured in early July.

For the September quarter, we expect capital spending to be $400 million to $450 million and we have debt maturities of $200 million net of the proceeds of the EETC we just issued. And we are forecasting $5.1 billion of unrestricted liquidity at the end of September quarter.

In conclusion, Delta had a successful June quarter. We produced an operating margin of 9.1%, generated a revenue premium to the industry for the 15th consecutive month, and had exceptional operating performance. We've made strategic investments in the business which will generate margin increases into the future, and we are implementing the structural initiatives we need to achieve better cost outcomes.

In conclusion as Richard and Ed mentioned earlier, these results would not have been possible without the hard work of our employees and all the momentum they've built into the business on all fronts.

Jill Greer

Thank you, Richard, Ed and Paul. Vicky, we're now ready to move to the questions from the analysts, so if you could please review the process for asking a question.

Question-and-Answer Session

Operator

Thank you, Ms. Greer. (Operator Instructions) We will take our first question from Glenn Engel of Bank of America.

Glenn Engel - Bank of America

Good morning. One cost question, one revenue question. On the cost side, the maintenance levels just, expense seems much higher than I would have expected. How long does it stay at these levels? In the second half, what do you

expect it to level out at and what's normal?

Paul Jacobson

Glenn, we continue to experience some pressure from seat-related modifications in the second quarter. We expect maintenance spend to be roughly flat for the rest of the year.

Glenn Engel - Bank of America

Flat with last year or flat with the first half?

Paul Jacobson

Flat with last year.

Glenn Engel - Bank of America

And second is the timing of the July 4 holiday seemed to have had an impact for some airlines. Can you say how much that probably held back your July PRASM?

Glen Hauenstein

This is Glen. Glenn, how are you?

Glenn Engel - Bank of America

Good.

Glen Hauenstein

July 4 with falling on a Wednesday is clearly not good for airline revenues. Business travel really took the whole week off. And because it was on a Wednesday, the discretionary traveler demand was not as high as it would have been had it been at the beginning or the end of the week. So it was, it's generally a bad week for us. This year it was particularly bad and probably had about a 0.3 to 0.4 point impact on the month.

Glenn Engel - Bank of America

Thank you very much.

Richard Anderson

Thank you, Glenn.

Operator

Next we'll hear from Savanthi Syth, Raymond James.

Savanthi Syth - Raymond James

Good morning. Just wondering on the $300 million savings you're expecting for the refinery, could you provide a little bit more about how you get that? Or if the details are a little complicated, what drives that? What are the key inputs that drive it and given where the fuel prices have been volatile and pulling down, does the benefit reduce if fuel prices pull back, or what are the kind of key inputs in getting that $300 million in savings a year?

Paul Jacobson

Savi, the $300 million in savings comes from the sale of the products in excess of the cost of manufacturing and cracking crude oil against the index prices that we've seen. And while there's been volatility in the crude oil markets, crack spreads have actually expanded slightly during that time period and we don't anticipate any change from our original guidance.

Ed Bastian

Savi, this is Ed. One other point is we talked about this when we announced the acquisition. We went, also back-tested this over the last six years and the average return Trainer would have had on our results is anywhere between $300 million and $500 million a year over the last six years. So we feel reasonably confident in our estimates on a going forward basis.

Savanthi Syth - Raymond James

Great. Just on my follow up question, have you kind of calculated what the contribution will be with the replacement of 717s with the – or with the 50-seaters and the kind of older aircraft and what the timing of that would be?

Ed Bastian

We haven't publicly disclosed the impact. Obviously we believe it to be substantial. If you look at the, not just the cost of continuing to keep the 50-seat RJs in the fleet but even more importantly the upcoming fairly significant maintenance costs that we're going to be experiencing which will run into the hundreds of millions of dollars on that fleet if we had decided to retain that aircraft. So not just a savings on the current cost structure but a substantial benefit to offset future cost rises.

Savanthi Syth - Raymond James

All right. Great. Thank you.

Operator

Next we'll hear from Jamie Baker with JP Morgan.

Jamie Baker - JP Morgan

Hey, good morning everybody. Ed, the 16% of corporate accounts that responded they would be flying less, any color on what type of business they fall into and is that 16% of respondents or 16% of your corporate revenue base?

Ed Bastian

It was 16% of our respondents. We took a very wide span of respondents and it lined up largely with the spend. And in any portfolio, you're going to have some guys that are increasing, some guys that are decreasing some of the sectors. You can guess yourself which are having more difficulty in this marketplace, particularly in the defense space. But on average, the trend lines are they're going to continue to stay with the spend patterns and the trends we've seen or actually look to expand it a bit going forward. So no unique comment in that 16%. I didn't see JPMorgan's results. So I don't know what they are telling you.

Jamie Baker - JP Morgan

Yes, to be decided. For Paul, the new pilot agreement includes a decrease in the profit sharing calculation. Is it reasonable to assume similar changes for non-union employees and if so, have those changes been made or should we leave the equation alone in our models for now?

Richard Anderson

Mike?

Mike Campbell

We have said to the non-union employees that the same adjustment in profit sharing will be made with them and that will be effective January 1 for next year.

Jamie Baker - JP Morgan

January 1. Okay, helpful. And lastly if I can squeeze one in for Richard. Once you get below the $10 billion net debt target, what's next?

Richard Anderson

What do you think should be next?

Jamie Baker - JP Morgan

Well I think the concern out there is that you're tempted to fall off the wagon and you go on some sort of a growth bender. That's not particularly my concern, but I hear it from investors all the time. On the other hand, there are pension issues that still need to be addressed. There's possible restoration of dividends, share buyback potential. I mean sort of take your pick and don't limit it to those.

Richard Anderson

Well first of all, we're not going to go – I mean I think we have demonstrated now for a number of years in a row a unique discipline around how we deploy our capital, and I think the 717 is a prime example of that and the MD-90 is a prime example of that. So we're not going to change that focus, because we think the most important thing we can do for our shareowners is de-risk and de-lever the business.

So we have some time to make that decision because we're scheduled to hit our net debt at $10 billion at the end of 2013. I think you can reasonably expect that no matter what we do, we're going to continue to grind down that net debt number, because that both improves our EPS quickly because it comes right out of non-op which benefits our shareholders significantly.

So I think no matter what, there are two principles and we have some time to discuss this with our investor base. But the first principle is we are not going to go, to use your term, we're not going on any benders around here, period, because we're incredibly focused on pay back of our capital investments and getting our ROIC target. And number two, you can count on us continuing to pay down debt in some form or fashion, even after we hit the $10 billion mark. Our ultimate goal, it's going to take us a while, is to get back to investment grade.

Jamie Baker - JP Morgan

Excellent. And you say take a while. Care to throw a year out there?

Richard Anderson

No, I don't care to throw a year out there.

Jamie Baker - JP Morgan

Okay. All right. Thanks for the clarity on that. That's a excellent response. I appreciate you letting me slide a third question in.

Richard Anderson

Do you have a fourth?

Jamie Baker - JP Morgan

No. That's okay. I'll turn it over to somebody else. Sorry.

Richard Anderson

I have another one for you. What's JPM's travel going to be? Are you going to try to get them to pick with us?

Jill Greer

I think she cut him off.

Operator

Next we'll hear from David Fintzen with Barclays.

Dave Fintzen - Barclays

Hey, good morning everyone. Just a question for Glen. You sort of mentioned the 5% premium on RASM that you're hitting today. I mean as you look out over the next couple of years with the puts and takes of the refleetings versus ongoing merger synergies on the revenue side, just how do you see that evolving? Is 105% your long term target in where you think you go or do you think there's upside from here on a relative basis?

Glen Hauenstein

We really believe that there's continued upside. The 105% is actually an amalgamation of all of the different entities, not all of which we have produced premiums today, but all of which we aspire to produce premiums over time and we think that that will drive the system-wide number higher over the longer term.

Dave Fintzen - Barclays

And so we should think of those as 105% sort of your target in every entity or in all – or is that, every entity has its own sort of expectation?

Glen Hauenstein

Every entity has its own expectations based on our gauge, our stage length, the market selections we fly. But I think it's safe to say that we think there is a couple of points of headroom, 2 to 3 points of headroom in the next couple of years that we could achieve.

Dave Fintzen - Barclays

Okay. That's helpful. And maybe a question for Richard, on your ROIC targets, just as you take a step back and think about the derisking and the deleveraging, and how should we think about ROIC over the cycle? I mean is that, is the range shrinking? Do you think 10% to 12% is achievable in most environments or do you think there's still a pretty wide range on returns through the cycle?

Richard Anderson

What we've been able to show, I think if you look at 2010, 2011, now 2012, we've been able to manage and have good performance and make good money through three years of pretty volatile fuel and economic environment. So that 10% to 12% return on invested capital we think is a solid number for us going forward. And this is a management team that is incredibly serious and intent on hitting that number for our shareowners.

Dave Fintzen - Barclays

Okay. Appreciate that color.

Operator

Next we'll hear from Michael Linenberg with Deutsche Bank.

Mike Linenberg - Deutsche Bank

Yes, hey. Just a couple here and I guess maybe a clarification. Richard, in your opening comments, when you talked about the third quarter and you mentioned bookings being good, I thought I heard 4% to 5% top line growth. Was that in reference to the third quarter?

Richard Anderson

No.

Ed Bastian

Mike that was month of July RASM.

Richard Anderson

Yes.

Mike Linenberg - Deutsche Bank

Okay, okay. All right, so that's helpful then. I guess next one for Paul Jacobson, you talked about the change in, or the RJ fleet, the shrinkage of that by 250 airplanes as being the single largest opportunity cost. And again I realize that there's been some questions on this maybe sort of variations on this, but how do we think about this? I mean you talked about hundreds of millions of maybe foregone maintenance expense on some of the older aircraft. What about the potential revenue opportunity? There are a lot of different moving parts on this. Any additional color that you could give us would be great.

Ed Bastian

Mike, I'll jump in. This is Ed. The revenue opportunity is substantial. We've said any number of times the 50-seaters have been the perfect storm for us because not only is it a cost opportunity, it's also an airplane our customers don't particularly prefer. So as we up-gauge, and that was sitting behind the 717 strategy and that's why they are linked at some level as well as getting some incremental two-class 76-seat RJs, we're going to have a fairly substantial up gauge in margin improvement, cost reductions, some revenue enhancements. And from the capital efficiency standpoint, with where we were able to acquire the 717s is going to improve those returns all the more. So it was a win all the ways around.

Mike Linenberg - Deutsche Bank

Okay. All right, thank you. Very good.

Operator

Next we'll hear from John Godyn with Morgan Stanley.

John Godyn - Morgan Stanley

Hi, everyone. Thanks for taking my question. Richard, when investors think of Delta, I think increasingly they look at you as aggressive and creative at trying to better manage or control some of the forces that other airlines leave to chance and maybe best symbolized by the recent refinery deal, and that's something you touched on in your prepared remarks. But as we think about scenarios surrounding American's emergence and the possibility of M&A, is this a situation where you think the outcomes are out of your control or does Delta have the ability to drive the situation toward outcomes it favors?

Richard Anderson

As a matter of policy, we do not comment or speculate on transactions of that nature. I would just say that overall, one, at Delta we will continue to always control our destiny. And by pushing a lot of different opportunities and leverage

across the business and, number two, global consolidation is good for the business model.

John Godyn - Morgan Stanley

Okay. That's helpful. And just broadly, we've heard from a lot of different airlines about solid revenue trends and how we're not seeing really any signs of economic weakness yet. But this quarter cargo revenue for you guys fell year-over-year for the second quarter in a row and we've seen a lot of weakness in cargo. Normally that's a canary in the coal mine. Can you help us understand why it makes sense to look through cargo weakness this time around when thinking about the trajectory of passenger revenue?

Ed Bastian

John, this is Ed. Cargo revenues for us in the second quarter were fairly flat on a year-over-year basis and we had some weakness in yields, but the volumes improved on a year-over-year basis. We're not a big enough cargo carrier to really be able to call that as a trend. Obviously we see what's going on with the bigger freight operators around the world. So I'd say, one, don't necessarily look at our cargo performance as a indicator.

But looking to our business model, we think when you're – because we've asked ourself that question a lot with some of the continued concerns and headline risk coming out of Europe and other parts of the geography, how do we look at our July unit revenue performance. And if you were to contrast June to July, there's about a 2 point sequential down-tick, which compared to what we would historically have expected to see. We think 1 point of the 2 point down-tick is due to some of the domestic competitive fare activities that we've commented on in the past.

And the other point is a myriad of a little bit of economic weakness, a little bit of the fuel sell-off which obviously has some revenue implications, a little bit of July 4. And again, just so a little bit of softening but nothing on the guise of what some of the cargo carriers are seeing. So, or a consumer business in the environment that we're operating in to see a 4 to 5 point year-on-year revenue improvement, which is our, effectively our same stores sales metric. We feel it's pretty solid.

John Godyn - Morgan Stanley

Okay, and can I ask just a quick clarification on an earlier question. There was a question about uses of cash and free cash flow. When you guys think about excess cash for paying down debt or what have you, is the right way to think about it as cash above and beyond the air traffic liability or do you define excess cash in a different way?

Paul Jacobson

We define excess cash as free cash flow, operating cash less capital investment.

John Godyn - Morgan Stanley

Okay. Thanks a lot.

Operator

Next we'll hear from Dan McKenzie with Rodman & Renshaw.

Dan McKenzie - Rodman & Renshaw

Hey, good morning everybody, thanks here. Ed, over what period of time is Delta targeting the $1 billion in cost savings and where does that leave the new non-fuel cost target? And then I guess related to that, how are you thinking about full year cost guidance at this point?

Ed Bastian

The $1 billion structural cost reduction is over the next two to three years, Dan, and obviously the 50-seat reduction is probably the single biggest contributor there. But the early retirement package that we just completed is also a contributor, so it will take a couple of years to see the benefits come through.

Dan McKenzie - Rodman & Renshaw

I see. And then I guess secondly here, if I can go back to revenues at 10% to 12% operating margin for the third quarter, of course is pretty encouraging. But the investor worry is just the daily barrage of negative economic data points and historically revenues at times have deteriorated quite quickly. I wonder if you could just talk about what's different today. Can you elaborate a little further about the source of confidence as you look ahead to demand in the back half of the year?

Glen Hauenstein

This is Glen. How are you doing?

Dan McKenzie - Rodman & Renshaw

Yes, thanks, Glen.

Glen Hauenstein

We don't have a crystal ball here and I think our commitment is to react as quickly as we can to changes in demand, and as we look out into the early fall, we really don't see anything yet. But that doesn't mean that we won't react quickly if we do see a shortfall. So I think our commitment to our shareholders and all of our constituents is to make sure we're doing the best we can with the information we have. And while we read the same headlines, right now in Europe we have a little bit of a disconnect between what we're experiencing and what you read in the headlines. So, and the forward bookings and forward unit revenues look great into the fall. If that starts to deteriorate, and so we have already taken proactive reductions. So we have reduced 5% of our capacity because of things we know. So we know the euro is lower and we know that winter is higher ex-European demand than ex-US demand which peaks in the summer. So we've already taken actions on what we know, and we will take the actions required as more unfolds if it does.

Dan McKenzie - Rodman & Renshaw

Okay, terrific. Thanks so much.

Operator

Next we'll hear from Helane Becker with Dahlman Rose & Company.

Helane Becker - Dahlman Rose & Company

Thanks very much, operator. Hi everybody. So just with respect to the changes you're going to make over on the regional side, one of your major providers is basically out there saying that there's no way you can get out of their contract, and the contracts go out four or five more years. And I'm just kind of wondering how we should think about that, given the fact that you've got to get down to something like 125 50-seaters over the next I think three years.

Richard Anderson

Well we have, without going into the particulars of any of the contracts that we have, we have a steady path to be able to get to 125. So we, without going into the specifics, we have a confident path of moving to the 125 and I'll just leave it at that.

Helane Becker - Dahlman Rose & Company

Okay. I will accept that. And then my other question is with respect to Latin American market. In the past couple of months, I've just seen some unit revenue growth slow. It hasn't been quite as robust as it was six or eight months ago. Is there anything accounting for that or is it just tougher comps which would be one thing to account for, I suppose. But is there anything going on we should know about?

Glen Hauenstein

This is Glen again. If you look to the fall, I think the one thing that we are keeping a close eye on is industry capacity. Clearly not Delta capacity, but as you get into the fall in Latin America, current schedules show that capacity is up around 10%. You combine that with decline of the local currencies, the real now, a lot of the real is not priced, the tickets aren't priced in reals but about 10% of our Brazilian sales for example are priced in reals and that has a 30% negative year-over-year bias. So I think you've got some foreign exchange. I think you've got some capacity issues. But I think the core demand is still quite strong.

Helane Becker - Dahlman Rose & Company

Okay. And then your investments in Aeromexico, where does that show up in the numbers, or does it?

Ed Bastian

It wouldn't show up, Helane, in the numbers per se. It would show up through better passenger revenues as we better hook our two networks up. You're not going to see that in a separate line item or anything.

Helane Becker - Dahlman Rose & Company

Okay, got you. Thank you.

Operator

Next we'll hear from Kevin Crissey with UBS.

Kevin Crissey - UBS

Hi. Thanks for taking my questions. CASM ex-fuel, I guess I just wanted to go back over the timeline a little bit. I think it was back say maybe October 2010, I think it was somewhere in that vicinity, you guys had targeted 2011 to be kind of flat with 2010. And then I think it was revised at your Investor Day and then you've cut some capacity. But what I'm trying to understand is, I didn't see these CASM ex-fuel pressures coming and I think I didn't see them partly because I think you guys had guided that they weren't really there or at least one point you had guided it that way, or maybe I'm misreading it. But I wanted to understand what changed from that point to today in terms of your pressure on the CASM ex-fuel line.

Richard Anderson

This is Richard. First, if you look out over the past two years, we have pushed capacity down pretty hard. We have viewed capacity as the real lever to push our business, and it has put real pressure on our non-fuel CASM. If you look where we'll be by the end of this year in 4Q and compare it to two years ago when we were giving that guidance, we're going to probably be down 5% to 6% in overall system capacity and the industry is probably on the main grown a bit. So if you think about being down 5% instead of being up 1% to 2% each of those two years, the equation is very much different on the nonfuel line.

The second piece is, is that we have along the way made investments that are the right investments in our product, in our employees, and you can see it in our revenue performance versus the industry. Hence our drive to drive another $1 billion of structural costs out and our push in the refinery to make up on a total basis, total unit cost basis, those inflationary pressures that we see.

Ed Bastian

And I'd say the other thing, Kevin, there that we did not necessarily forecast or see coming as clearly is the opportunity we had with our pilots to do the contract early. It's going to pay significant dividends over time as it will have a big cost return to it, not just in terms of improved productivity, but the ability to fairly substantially restructure the domestic fleet. But that those costs came in right away so that's in our September guidance as well, and that was another big piece.

Kevin Crissey - UBS

Okay. Thank you. And Richard maybe if I think about, you talk about derisking the business and we all want that, one of the big things as we look across transportation companies, fuel is only a discussion in the airlines pretty much. If you

look at trucking or rails and stuff, what more can be done to allow fuel surcharges to truly be pass-throughs? I mean it should be to me, it should be the effort that's expended by every company before they buy more planes, it's like let's see how we can get a fuel surcharge in here that actually truly does what it does in every other industry.

Richard Anderson

Two points there that are different in this industry from those industries, which is we sell our tickets 330 days in advance. So if at the point in time that we sell the ticket for travel six months from now, we don't have – we have current fuel or the current forecast that we have for fuel which we use in our pricing department.

Because, if you look at businesses in a totally deregulated environment that are commodity intensive, the management team is always working to match the cost of production to the pricing in the marketplace. We're a bit more challenged in that we sell tickets 330 days in advance and the DOT does not allow us to collect fuel surcharges in the US. We can inform point of sale but we cannot in the US.

So there are some differences there. So what we do is we manage capacity very tightly and are prepared to suffer some of the risks of a little higher unit cost creep as a result because the independent variable needs to be then how we manage our capacity and how we manage our internal pricing mechanisms to be certain that our prices are capturing the actual cost of goods sold at the time that we price.

And that leads me to my second point which is why we hedge fuel. Because if you're selling 330 days in advance and you cannot legally use fuel surcharges, we need the ability to take some of the volatility out and allow us in a more near term basis to lock in our margins.

And candidly, that's what we just did in the second quarter. When we were moving through the second quarter, we saw some of the best revenue performance we've ever seen for the month of May, and but the biggest risk was where fuel was going in the January through April timeframe. And we wanted to be certain that we had 200 basis points of margin expansion. So it's going to be a combination of, one, managing your capacity, because that's our biggest lever. And we're going to continue to manage the capacity to be able to drive our revenue up by putting more revenue on each airplane and you do that by reducing capacity.

The second thing is, in our pricing environment, we're very focused on having our pricing and yield management professionals have the cost data at the time they make decisions around capacity and pricing. Third, we made an investment in the refinery to be able to take the crack spread risk out of our business, which is our single highest fuel expense. And number four, to use our hedging program in the shorter term to be able to lock in our margins, so that we know that our cost of goods sold is going to match the pricing we have in the market.

Kevin Crissey - UBS

Thank you. Just one last real fast one because Jamie had three, I'll take three. Capacity change by month, if you could to help us frame the RASM expectations by month?

Ed Bastian

There's nothing – we don't typically give the monthly forward capacity outlooks, Kevin, but there's nothing unique in the months.

Kevin Crissey - UBS

Okay. Thank you.

Jill Greer

Vicky, we're going to have time for one more question from the analysts.

Operator

Okay. We will take our question from Hunter Keay with Wolfe Trahan.

Hunter Keay - Wolfe Trahan

Thanks for getting me in, appreciate it. Just maybe a subtlety, Richard, but you've referred to a net debt target of $10 billion by the end of 2013. I think recently you guys have been saying mid-2013. Is there any particular reason why that's changed? Given I think the pull back in the fuel prices, I would have thought maybe that could have been possibly even accelerated a little bit. Is that, just any kind of color on that would be great.

Richard Anderson

No, there's no change. Our goal is to make certain that we get it done as soon as possible.

Hunter Keay - Wolfe Trahan

Sure, okay thanks. And a little bit more on the hedge book. Can you tell us how you manage the risk or oversee the tail risk in the hedge book? Because we obviously saw some pretty big mark to market adjustments with the big pull back in prices in May and I'm wondering how you guys think about managing risk within the derivative exposure in the hedge book. Who oversees it, what's your sort of tolerance threshold for risk? Any kind of color you could share with us would be great.

Paul Jacobson

Hunter, this is Paul.

Hunter Keay - Wolfe Trahan

Hey Paul.

Paul Jacobson

We have a robust and independent risk management function that oversees the financial risks of the company including the hedging book. When we hedge fuel and we see rapid declines in fuel prices, you're going to expect hedge losses because the hedge book is net long in its offsetting position. But we monitor that very independently and we're very comfortable with our position in our book.

Hunter Keay - Wolfe Trahan

Okay. Thank you.

Jill Greer

Vicky, that is going to conclude the analyst portion of the call and so I'm going to turn it over to Ned Walker, our Chief Communications Officer for the media portion.

John Walker

Okay hey, thanks very much, Jill, and welcome everybody. Vicky, we're ready to begin the Q&A with the media. We'll ask the media to limit themselves to one question with a quick follow-up. We should be able to accommodate most Q&As but often we are not able to get everybody on. So with that we'll go ahead and turn it over to the first question, please.

Operator

Thank you. Again, that concludes the analyst portion of the question and answer session. We will now take questions from the media. (Operator Instructions) We'll take our first question from Mary Schlangenstein with Bloomberg News.

Mary Schlangenstein - Bloomberg News

Quick question. Earlier in the call, you said that you are looking at other initiatives like the refinery to decrease your fuel exposure. And I wanted to see if you could be any more specific in terms of what you might be looking at.

Richard Anderson

I thought we were fairly clear in saying that the way we manage our fuel exposure is, one, capacity; number two, having the right pricing processes and mechanisms in the company to be certain that we're fully covering the cost of fuel in our pricing; number three, we have a lot of fuel efficiency efforts under way, including our refleeting, adding winglets and more efficient aircraft routings; and then number four is our hedge program.

Mary Schlangenstein - Bloomberg News

I'm sorry. I thought the reference was perhaps to another asset purchase of some kind?

Richard Anderson

No, that was not what the reference was at all.

Mary Schlangenstein - Bloomberg News

Okay. Thank you.

John Walker

Thanks, Mary.

Operator

Next we'll hear from Andy Compart with Aviation Week.

Andy Compart - Aviation Week

Richard, I want to get back to the steady path to 125 50-seaters. SkyWest's CFO, which was an indirect reference made to earlier, had said to me that they operate about 150 50-seaters and he said they are not inclined to trade them for 76-seater, two-class 76 seaters if there's nowhere to put the 50-seater. So that's above 125 right there. so how do you get to that if SkyWest or others are resistant to making this trade-off?

Richard Anderson

I'm going to stand on what I said before which is we have a clear path through – we have a number of operators and a number of contract expirations and I think we've shown a pretty steady process here. I mean our high watermark was a little over 500 and I think today we're at 300, 320. So we've been able to do 180 so and I think you just have to stay tuned, but it's going to happen.

Andy Compart - Aviation Week

Can you do it without voluntary participation by some of the partners?

Richard Anderson

As I said, I mean without going into the specifics of any of these, it is going to happen.

Andy Compart - Aviation Week

All right. Thanks.

John Walker

Thanks Andy. Vicky, next question.

Operator

Next we'll hear from Josh Freed with The Associated Press

Josh Freed - The Associated Press

Yes, well I suppose this is related. What can you tell us today about your plans for Comair?

Richard Anderson

In view of the significant changes in the economic and competitive conditions in the regional airline industry in recent years, Delta continues to explore strategic alternatives for Comair as previously announced. Until a final decision has been made, we cannot comment further.

John Walker

Hey, thanks Richard that was really good.

Josh Freed - The Associated Press

It almost felt like you were reading from something there.

John Walker

No, that's really, Josh, that's really basically been what we've been telling you and the rest of the media over the last few weeks and so our position really hasn't changed publicly on that.

Josh Freed - The Associated Press

All right. Thank you.

Operator

Next we'll hear from Kelly Yamanouchi with The Atlanta Journal-Constitution.

Kelly Yamanouchi - The Atlanta Journal-Constitution

Hi there. I'm just wondering, since you have a target of $1 billion in structural cost reduction over the next few years, do you plan for further job cuts over that period to accomplish that?

John Walker

No.

Kelly Yamanouchi - The Atlanta Journal-Constitution

All right. Thank you.

Operator

Next we'll hear from Edward Russell with Flight Global.

Edward Russell - Flight Global

Yes, hi. I was wondering if you could detail a bit more the swap from 50-seaters to 76-seaters at your regional carriers about who might be receiving those and where they might be going?

Richard Anderson

No, we wouldn't comment on that. We've got a lot of work to do there and there will be RFP processes and the like so we can't comment on that. We'll let you know as soon as it's all worked out.

Edward Russell - Flight Global

Okay. Thank you.

John Walker

Okay Vicky, we have time for one more question

Operator

Okay, we will take that question from Linda Loyd with Philadelphia Inquirer.

Linda Loyd - The Philadelphia Inquirer

Thank you for taking my call. I have two questions about the Trainer refinery. How is the turnaround at Trainer going at this point, and do you anticipate you will have to spend more than the estimated $100 million to get the refinery up and running?

Paul Jacobson

This is Paul Jacobson. The turnaround is actually progressing very, very well. We are on budget and on target to begin restarting that facility in mid-September, and we expect the actual costs to come in line with all of our expectations. There have been no surprises.

Linda Loyd - The Philadelphia Inquirer

Well thank you, and I have one follow-up question. How many years are the swaps with BP and Phillips 66? That's the first part of that, and what are Delta's plans after those swaps expire?

Paul Jacobson

Those are, all the commercial agreements that we entered into are three-year agreements and we'll continue to monitor that as we get underway and down the road and explore our options.

Linda Loyd - The Philadelphia Inquirer

Because it is not true that the benefits of buying the refinery hinges on the swaps for the gasoline and diesel produced at Trainer for jet fuel that is made somewhere else?

Paul Jacobson

No, the swaps are a means to exchange product for jet fuel. The economics of the transaction don't hinge on those commercial agreements but they are sources for those products and there's a broad market for those products in that area.

Linda Loyd - The Philadelphia Inquirer

Okay. Thanks very much.

John Walker

Okay thank you very much, Richard, Ed and Paul. That concludes our June quarter call. We'll be back in three months with the September quarter. Thanks very much.

Operator

Again that does conclude today's teleconference. Thank you all for joining.
